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SUBJECT: A TALE OF TWO CRISES: SENIOR BELGIAN FINANCE MINISTRY OFFICIAL ON THE FINANCIAL CRISIS AND BELGIUM'S ON-GOING POLITICAL CRISIS

Classified By: POL/E Counselor Richard Eason

¶1. (C) SUMMARY: At one point in the middle of the on-going crisis in Belgium's banking sector, according to a top Finance Ministry official, Belgium narrowly avoided a bank run. The financial crisis is already being used by the francophone socialists against the francophone liberals who control the finance ministry, despite both being in the ruling government coalition. The financial crisis, which hits the wallets of every Belgian, has pushed the stalemated institutional talks far off center stage. The crisis is also wreaking havoc with the government's budgeting process, with deficits now being unavoidable for both 2008 and 2009. END SUMMARY.

AND THEN THERE WAS ONE...

¶2. (C) Olivier Henin, top aide to Belgium's Finance Minister, told visiting EUR/WE Deputy Director and emboffs on October 17 that the financial crisis in Belgium has pushed all other issues off center stage. The months-long debates on institutional reforms have been shelved for now. The financial crisis is hitting every Belgian's savings and the continuing rescues of the country's two top banks are riveting everyone's attentions. Henin said that Fortis, the first bank to need rescue, had been the bank of the establishment. Its collapse and dismemberment was a trauma to many Belgians. For years, Fortis had been seen as Belgium's bluechip investment. Families passed down their shares from generation to generation as a nest egg. Henin asserted that the savings were safe but that shareholders could not expect the government to do anything about the collapse in the share prices.

¶3. (C) Henin attributed Fortis' failure to three factors: poor management, the systemic collapse in market confidence, and the purchase of ABN AMRO last fall when markets were at their peak. When share prices fell and credit dried up, Fortis could no longer finalize the deal and begin to try to build synergies with the parts of ABN AMRO it had acquired.

¶4. (C) Belgium had narrowly avoided a bank run (a clear reference to Fortis), Henin said. During the weekend, when the Finance Ministry was working out a rescue package with the Fortis partners, Ministry officials even feared an internet run on the bank through its pc banking services. Fortunately, the run did not happen. But the government had to turn its attention immediately to Dexia, Belgium's second largest bank. (NOTE: Belgium's third largest bank, KBC, though under pressure for a time due to unfortunate remarks by the governor of Belgium's Central Bank, has less exposure to subprime loans and is stable. END NOTE.).

SO MUCH FOR THE BALANCED BUDGET

¶5. (C) The uncertainty generated by the financial crisis

has led to estimates of Belgium's growth for 2009 that range from 0.2% to 1.2%. If the growth rate ends up closer to the lower end of the range, significant budget deficits will result. The budgets for 2008 and 2009 are also reliant on significant transfers (500 million euros) from the regions (largely Flanders) and a 250 million transfer from the energy sector in exchange for (perhaps) extending the phase-out of the country's nuclear power plants from 2015 to some unspecified later date. Neither of these options are guaranteed to play out.

HITTING THE REAL ECONOMY

¶6. (C) Henin said the Finance Ministry was receiving many letters of complaint from people lamenting their inability to obtain credit. Henin said that the banks would be unable to lend to anyone unable to qualify and that the banking system had no choice but to return to fundamentals of risk analysis for lenders.

FROM BRUSSELS TO LUXEMBOURG TO REKYAVIK

¶7. (C) Like thousands of British investors, there were Belgians caught up in the collapse of Iceland's banking system. According to Henin, there were 20,000 Belgian account holders with money in the Luxembourg branch of an Icelandic bank.

WAITING FOR FLEMISH "POLITICAL RESPONSIBILITY"

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¶8. (C) Turning to politics, Henin referred to the break-up of the Belgian nationalist party years ago to political sub-prime debt. Those who left that party went to many different Belgian parties, including the NVA, and its is many of those voices who are now driving the debate on institutional reforms. Reflecting his francophone constituency (Liberals or MR), Henin said that the francophone parties are still waiting for a demonstration of "political responsibility" by Flanders with regard to serious treatment of institutional reform. According to Henin, for the francophone parties, everything connected with institutional reform is on the table.

¶9. (C) However, for the moment, managing the country's financial crisis is taking center stage. The francophone socialists (PS) are using the crisis to play on the fears of citizens, as an attempt to strength its intense competition with MR in Wallonia (with regional elections looming next June). Henin is not sure the whether the PS tactics will work and he fears that MR could fall back to its considerably lower vote totals of 2004, benefiting PS instead.

COMMENT

¶10. (C) Few Belgians supported their political elite in their squabbling over political issues over the past year. Now everyone's attention is riveted on the country's banking and financial crisis. Banks that even older Belgians had grown up with are now gone or changed irrecognizably. KBC is the only remaining large Belgian-owned bank. Many Belgians own shares in these banks and have seen the values of their portfolios plummet. After months of continuing revelations of further write-downs and the need for new capital injections, there is little confidence left in the country's financial sector and it will take a very long time to restore it.

¶11. (C) In the meantime, the crisis could well give a significant push to the socialists in Belgium, particularly in Wallonia. Didier Reynders, head of the francophone

liberal MR party, has been Finance Minister for nine years. In the 2007 federal elections, his party benefited from well-publicized corruption scandals involving the PS in Wallonia. Barring some new scandal, MR will find itself in a tough battle with PS in the June 2008 regional elections ..